

Message Text

SECRET

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S E C R E T SECTION 1 OF 2 JIDDA 0453

NODIS

E.O. 11652: GDS
TAGS: ENRG, US, SA
SUBJECT: SECRETARY SCHLESINGER'S CALL ON MINISTER OF PET-
ROLEUM YAMANI ON JANURAY 14,1978

1. SECRETARY SCHLESINGER MET WITH MINISTER OF PETROLEUM AND MINERALS ZAKI YAMANI IN RIYADH ON JANUARY 14. ALSO PRESENT WERE AMBASSADOR WEST, ASST SEC BERGOLD, DEPUTY ASST SEC BOSWORTH, AND DCM WILEY ON THE U.S. SIDE, AND DEPUTY MINISTER TURKI AND DIRECTOR GENERAL OF PETROMIN TAHER ON THE SAUDI SIDE. THE FOLLOWING ACCOUNT OF THE CONVERSATION HAS NOT BEEN CLEARED BY SEC. SCHLESINGER OR ANY MEMBER OF HIS PARTY.

2. AFTER THE OPENING PLEASANTRIES, YAMANI SAID THAT THE U.S. WAS LAGGING IN TAKING THE NECESSARY CONSERVATION MEASURES ON THE USE OF ENERGY. SECRETARY SCHLESINGER REPLIED THAT PRESIDENT CARTER HAS PLACED HIS PRESTIGE ON THE LINE IN PROMOTING CONSERVATION BUT, UNFORTUNATELY, ENERGY PROBLEMS HAVE BEEN MANIPULATED IN THE PAST AS POLITICAL FOOTBALLS. AS A RESULT THERE IS NOW A FAIR AMOUNT OF DISTRUST AMONG THE GENERAL PUBLIC AND THIS MAKES IT MORE DIFFICULT FOR THE CONGRESS TO PASS MEANINGFUL LEGISLATION. NEVERTHELESS, WE WILL GET A BILL IN ANOTHER MONTH OR TWO WHICH WILL NOT IN ITSELF BE ENOUGH BUT WILL
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BE A BIG IMPROVEMENT OVER WHAT WE HAVE DONE IN THE PAST. THIS BILL SHOULD BE CONSIDERED AS PHASE ONE. IT DEALS PRIMARILY WITH TAXING AND PRICING POLICIES THAT WILL ESTABLISH A FRAMEWORK FOR THE NEXT PHASE. THE NEXT PHASE WILL EMPHASIZE THE DEVELOPMENT OF NEW TECHNOLOGIES FOR THE PRODUCTION OF ALTERNATIVE SOURCES OF ENERGY AND FOR THE MORE EFFICIENT UTILIZATION OF ENERGY SUPPLIES. WE THOUGHT

THAT IT WAS BETTER NOT TO MIX THESE TWO AT THE PRESENT TIME BECAUSE THERE ARE SOME CONGRESSMEN WHO HAVE SPECIFIC OBJECTIONS TO CERTAIN ASPECTS OF THE NEW TECHNOLOGY. IN FACT, WE ARE OPTIMISTIC ON COAL GASIFICATION. WITH A LITTLE LUCK WE SHOULD BE ABLE TO PRODUCE THE EQUIVALENT OF 500,000 BARRELS PER DAY OF OIL BY 1982 USING COAL GASIFICATION TECHNIQUES. AFTER THAT WE HOPE THAT SHALE OIL AND NATURAL GAS CAN GRADUALLY BE BROUGHT INTO THE ENERGY PICTURE TO PICK UP THEIR SHARE OF THE LOAD.

3. IN GENERAL, SCHLESINGER CONTINUED, U.S. ATTITUDES TOWARDS THE USE OF ENERGY ARE IMPROVING BUT PUBLIC OPINION CANNOT BE CHANGED INSTANTANEOUSLY. HOWEVER, OPINION HAS CHANGED MORE DURING THE PAST YEAR THAN IN THE PREVIOUS THREE OR FOUR YEARS.

4. MINISTER YAMANI THEN ASKED ABOUT THE PROBLEMS OF POLLUTION THAT WOULD ARISE FROM THE USE OF COAL. SCHLESINGER REPORTED THAT COAL TECHNOLOGY IS IMPROVING BUT SOME RELAXATION OF STANDARDS WILL PROBABLY BE REQUIRED. THE SITUATION DOES NOT REQUIRE WHOLESALE RELAXATION, BUT SOME OF THE MORE RESTRICTIVE ASPECTS OF CURRENT CONSERVATION POLICIES MAY HAVE TO BE MODIFIED. YAMANI THEN ASKED IF THE USG WILL BE ABLE TO CUT IMPORTS OF CRUDE OIL TO SIX MILLION BARRELS PER DAY AS ADVOCATED BY PRESIDENT CARTER. SCHLESINGER REPLIED THAT IF MINISTER YAMANI WERE
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SKEPTICAL ABOUT THIS TARGET FIGURE, HIS SKEPTICISM WOULD BE JUSTIFIED. IN FACT, A TARGET FIGURE OF EIGHT AND ONE-HALF TO NINE MILLION BARRELS PER DAY OF IMPORTS BY THE YEAR 1985 MAY BE MORE JUSTIFIED. NEXT YEAR WE HOPE THAT THE UNITED STATES CAN REDUCE ITS IMPORTS TO THIS LEVEL. A MAJOR EFFORT WILL BE REQUIRED TO HOLD TO THIS TOTAL IN COMING YEARS. THE SIX MILLION BARRELS PER DAY GOAL, HOWEVER, IS A GOOD FIGURE TO SET UP AS A GOAL AND WE WILL CONTINUE TO USE IT AS A MEANS OF BRINGING PRESSURE TOWARDS FURTHER CONSERVATION OF ENERGY RESOURCES.

5. SCHLESINGER THEN ASKED WHAT THE UNITED STATES CAN NOW DO FOR SAUDI ARABIA. YAMANI REPLIED THAT WE COULD TAKE MEASURES TO REDUCE CONSUMPTION AND TO DEVELOP ALTERNATIVE ENERGY SOURCES. WE COULD ALSO HELP SAUDI ARABIA BUILD A TECHNOLOGICAL BASE FOR ITS OWN INDUSTRIALIZATION PROGRAM. IN PARTICULAR, WE COULD START WITH THE PROBLEM OF DEVELOPING THE NEEDED MANPOWER FOR INDUSTRY. SAUDI ARABIA NEEDS BOTH TECHNOLOGY AND MARKETS TO DISPOSE OF THE PRODUCTS OF THE NEW TECHNOLOGY. THE SECRETARY THEN ASKED WHAT IT WAS SPECIFICALLY THAT SAUDI ARABIA WOULD LIKE TO RECEIVE FROM THE U.S. TO ASSIST IT IN THE TRANSFER

OF TECHNOLOGY. YAMANI MENTIONED TAX PROBLEMS, PARTICULARLY THE TAXATION OF INDIVIDUAL AMERICANS, WHICH ARE NOW MAKING IT DIFFICULT FOR SAUDI ARABIA TO STRUCTURE JOINT VENTURES WITH AMERICAN FIRMS.

6. YAMANI THEN ASKED ABDUL HADI TAHER, THE DIRECTOR GENERAL OF PETROMIN, TO COMMENT ON THE PROBLEMS OF TECHNOLOGICAL TRANSFER. TAHER SUGGESTED THAT THERE WERE CERTAIN LEGAL PROBLEMS THAT PROHIBIT AMERICAN COMPANIES FROM ENTERING INTO LEGAL RELATIONSHIPS WHICH SAUDI ARABIA WOULD LIKE IN CERTAIN CIRCUMSTANCES, FOR INSTANCE, THERE ARE SOME SITUATIONS WHERE THE TAX LAWS MAKE IT ADVISABLE FOR AMERICAN COMPANIES TO COME TO SAUDI ARABIA IN JOINT VENTURE ARRANGEMENTS WITH SAUDIS RATHER THAN AS
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CO-OWNERS OF A SINGLE COMPANY. TAHER COMMENTED THAT SOME AMERICAN COMPANIES SEEM QUITE RELUCTANT TO LICENSE TECHNOLOGY EXCEPT THROUGH THE JOINT VENTURE MECHANISM. TAHER ALSO SAID THAT HE THOUGHT IT IMPORTANT THAT THE TRANSFER OF TECHNOLOGY BE INSTITUTIONALIZED TO A GREATER EXTENT THAN IT HAS BEEN IN THE PAST. HE POINTED OUT THAT THE JOINT COMMISSION NOW FUNCTIONS PRIMARILY AS A GOVERNMENT-TO-GOVERNMENT ORGANIZATION AND THAT IT IS CONSEQUENTLY NOT INVOLVED IN MANY OF THE IMPORTANT ISSUES OF TECHNOLOGICAL TRANSFER WHICH ARE OF CONCERN PRIMARILY TO THE PRIVATE SECTOR. THE SECRETARY COMMENTED THAT SOME PETRO-CHEMICAL CONCERNS MAY BELIEVE THAT CAPACITY IN CERTAIN LINES IS BEING OVER BUILT BUT HE AGREED THAT WE MAY NEED SOME MORE EFFECTIVE BILATERAL INSTITUTIONS TO DEAL WITH THE PROBLEMS OF TECHNOLOGICAL TRANSFER. AMBASSADOR WEST COMMENTED THAT HE HAD HEARD SOME COMPLAINTS ABOUT THE OPERATIONS OF THE U.S. - SAUDI JOINT COMMISSION. SOME PEOPLE HAD SAID THAT THERE WAS TOO MUCH EMPHASIS ON PLANNING WITH TOO LITTLE ACTION.

7. YAMANI MENTIONED THAT SAUDI ARABIA HAS HAD GOOD EXPERIENCE IN THE MINERALS FIELD IN WORKING WITH THE U.S. GEOLOGICAL SURVEY AND IN THE PETROLEUM FIELD THROUGH ARAMCO. HE ADDED, HOWEVER, THAT THERE IS NO REAL TECHNOLOGY IN SAUDI ARABIA AT THE PRESENT TIME. SAUDI ARABIA NOW MUST START TO DEVELOP ITS OWN TECHNOLOGY BUT IS NOT YET IN A POSITION TO FUNCTION AS A FULL PARTNER WITH ADVANCED TECHNOLOGICAL SOCIETY SUCH AS THE UNITED STATES.

8. SCHLESINGER THEN MENTIONED THAT SOLAR ENERGY IS ESSENTIALLY A LONG-TERM PROPOSITION. WE ARE STILL IN THE PRELIMINARY STAGES AND DO NOT FORESEE A RAPID DEVELOPMENT OF SOLAR ENERGY AS AN ALTERNATIVE ENERGY SOURCE. WE DO SEE SOME PROGRESS IN THE AREA OF BETTER UTILIZATION
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OF WOOD AND ANIMAL WASTES AS ENERGY SOURCES. WE ALSO BELIEVE THAT PHOTO-VOLTAIC DEVELOPMENTS LOOK RATHER INTERESTING, PARTICULARLY IN REMOTE LOCATIONS. EVEN THERE, HOWEVER, IT WILL BE NECESSARY TO REDUCE COSTS CONSIDERABLY TO PRODUCE PHOTO-VOLTAIC CELLS THAT COULD COMPETE WITH MORE CONVENTIONAL SOURCES OF ENERGY.

9. SCHLESINGER SAID THAT HE BELIEVED THAT THERE HAS BEEN A CERTAIN AMOUNT OF MYTHOLOGY IN THE UNITED STATES ON THE EXTENT TO WHICH SAUDI ARABIA COULD GO TO SATISFY OUT ENERGY APPETITES. SOME OF THE PREDICTIONS OF POTENTIAL OIL PRODUCTION FROM SAUDI ARABIA ARE QUITE UNREALISTIC. YAMANI REMARKED THAT THERE IS STRONG RESISTANCE IN SAUDI ARABIA TO FURTHER EXPANSION OF OIL PRODUCTION. THE ADVOCATES OF THIS POSITION ARGUE THAT SAUDI ARABIA IS NOW DEPLETING ITS ONLY RESOURCE AT THE EXPENSE OF FUTURE GENERATIONS. IN RETURN FOR ITS PRODUCTION IN EXCESS OF CURRENT CASH NEEDS, SAUDI ARABIA IS ACCUMULATING DOLLAR DENOMINATED INVESTMENTS THAT LOSE VALUE STEADILY AS A RESULT OF RAMPANT WORLDWIDE INFLATION. IN FACT, THE OIL IN THE GROUND WOULD PROVIDE A MUCH BETTER INVESTMENT

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MEDIUM FOR SAUDI ARABIA THAN BANK DEPOSITS OR U.S. GOVERNMENT BONDS. OTHERS, HOWEVER, ARGUE THAT A WORLDWIDE RECESSION WOULD NOT BE IN SAUDI ARABIA'S INTEREST AND ADVOCATE SOME INCREASED PRODUCTION, WITHIN REASON, TO

PROVIDE FOR THE WESTERN WORLD'S BASIC ENERGY REQUIREMENTS. YAMANI SAID HIS PERSONAL IMPRESSION IS THAT THERE WILL BE SOME INCREASE BUT THAT PREDICTIONS OF 18 MILLION BARRELS PER DAY OR EVEN 16 MILLION BARRELS PER DAY IN THE MID-80'S ARE NOT REALISTIC. SECRETARY SCHLESINGER SAID THAT AS A PRACTICAL MATTER A FREEZE IN SAUDI PRODUCTION WOULD CREATE DISRUPTION IN THE FREE WORLD AND PROBABLY PROVIDE FOR A GROWTH OF WORLDWIDE SOVIET POWER.

10. SCHLESINGER SAID HE PERSONALLY THOUGHT IT WAS UNFORTUNATE THAT THE CIA HAD PUBLISHED ITS STUDY. THE STUDY WAS A TECHNICAL EXAMINATION OF FUTURE DEMAND AND SUPPLY TRENDS BUT WAS NOT A POLICY DOCUMENT. IN FACT, THE LEVELS OF PRODUCTION MENTIONED IN THE STUDY FOR SAUDI ARABIA ARE NEITHER ATTAINABLE NOR DESIRABLE. OUR PROBLEM IS TO SHAPE EXPECTATIONS INTO A MORE REALISTIC FRAMEWORK. THE QUESTION IS NOW WE CAN ALTER ATTITUDES IN ORDER TO CREATE EXPECTATIONS THAT ARE WITHIN THE BOUNDS OF REALITY.

11. YAMANI SAID THAT TOO MUCH TALK ABOUT OIL PRODUCTION
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AT THE PRESENT TIME IS NOT HELPFUL. IT WOULD NOT NOW BE WISE FOR THE USG TO TACKLE THIS PROBLEM HEAD ON. YAMANI THEN ASKED FOR SCHLESINGER'S VIEWS ON SUPPLY AND DEMAND IN THE COMING TWO YEARS. SCHLESINGER REPLIED THAT OPEC WILL PROBABLY PRODUCE 31 TO 32 MILLION BARRELS PER DAY UNTIL 1980. THE EXPANSION OF CAPACITY IN THE NORTH SLOPE, THE NORTH ATLANTIC, AND IN MEXICO SHOULD TAKE CARE OF ANY INCREASED REQUIREMENTS FOR WESTERN ECONOMIES DURING THE NEXT TWO YEARS. IN FACT, THE WESTERN ECONOMIES ARE NOT GROWING VERY RAPIDLY. THIS WILL, OF COURSE CONSTRAIN THEIR DEMAND FOR OIL, BUT IT MAY ALSO CREATE SOME POLITICAL DIFFICULTIES SUCH AS WE ARE NOW SEEING IN ITALY.

12. SCHLESINGER THEN COMMENTED THAT SOVIET EXPERTS TO EASTERN EUROPE WILL PROBABLY SOON BEGIN TO DECLINE. ALREADY POLAND AND CZECHOSLOVAKIA HAVE BEEN TOLD TO FIND THEIR OWN OIL SUPPLIES. BY 1985 EASTERN EUROPE SHOULD BE BUYING AT LEAST TWO MILLION BARRELS PER DAY FROM WESTERN MARKETS.

13. SCHLESINGER THEN OFFERED TO PROVIDE A CLASSIFIED BRIEFING ON SOVIET OIL PRODUCTION AND ENERGY REQUIREMENTS TO YAMANI THE NEXT TIME YAMANI COMES TO THE UNITED STATES. SCHLESINGER SAID THAT WE HAD EVIDENCE THAT THE SOVIET LEADERSHIP HAS RECENTLY BECOME CONCERNED ABOUT THEIR ENERGY SUPPLIES. THEY, TOO, WILL UNDERTAKE CONSERVATION MEASURES AND WILL PROBABLY ATTEMPT TO SUBSTITUTE NATURAL

GAS FOR OIL. HOWEVER, THEY HAVE TECHNICAL PROBLEMS. THEY HAVE OVER-PRODUCED THEIR FIELDS AND THEY HAVE NOT DONE ENOUGH EXPLORATION. THEIR TECHNOLOGY IS 20 TO 25 YEARS BEHIND THAT OF THE WEST.

14. YAMANI THEN ASKED ABOUT THE CONSEQUENCES OF THE
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POTENTIAL SOVIET ENERGY SHORTAGE FOR SOVIET FOREIGN POLICY. SCHLESINGER POINTED OUT THAT THE SOVIET UNION IS LOCATED NEAR THE GULF AND NEAR IRAN. WE CAN ALSO EXPECT A CHANGE IN THE SOVIET LEADERSHIP TO A YOUNGER AND PERHAPS LESS CAUTIOUS GROUP OF MEN THAN THOSE NOW RUNNING THE COUNTRY. SUDDEN AND SERIOUS ENERGY PROBLEMS COULD RESULT IN MORE THREATENING BEHAVIOR BY THE SOVIET UNION. YAMANI THEN POINTED OUT THAT THE SOVIET UNION PROBABLY HAS ACCESS TO IRAQI OIL AND IRAQ HAS SOME VERY SUBSTANTIAL RESERVES. IF THE SOVIETS CAN OBTAIN MORE OIL FROM IRAQ, THIS SHOULD GO AT LEAST PART WAY IN SATISFYING THEIR REQUIREMENTS. SCHLESINGER REPLIED THAT THESE PROBLEMS NEED FURTHER ANALYSIS AND DISCUSSION. THE SOVIET UNION MAY HAVE LARGE PETROLEUM RESERVES, BUT THEY HAVE NOT MADE ADEQUATE EFFORTS TO EXPLORE THEM.

15. YAMANI THEN MENTIONED THE LAST OPEC CONFERENCE AND THE SAUDI ROLE IN FREEZING OIL PRICES. HE SAID THAT HE HOPED THAT THIS ACTION HAD NOT BEEN A MISTAKE. HE WAS AFRAID, HOWEVER, THAT AN OIL PRICE FREEZE NOW MIGHT RESULT IN LARGER INCREASES LATER ON. THIS WOULD BE MORE DIFFICULT FOR THE WESTERN ECONOMIES TO DIGEST THAN A SERIES OF SMALLER INCREASES. YAMANI ASKED SCHLESINGER IF A SERIES OF SMALL INCREASES WOULD NOT BE BETTER THAN A FEW LARGE JUMPS. SCHLESINGER REPLIED THAT THIS IS A QUESTION OF WEIGHING LONG-TERM BENEFIT AGAINST SHORT-TERM BENEFIT. IN THE SHORT RUN IT IS CLEARLY TO THE ADVANTAGE OF THE WESTERN ECONOMIES FOR THE CURRENT PRICE TO REMAIN AS LONG AS POSSIBLE AT THE PRESENT LEVEL. THIS WILL HELP ITALY AND FRANCE IN PARTICULAR IN DEALING WITH THE CHALLENGE OF THEIR COMMUNIST PARTIES. YAMANI REPLIED THAT WHEN THE SUPPLY-DEMAND SITUATION CHANGES, NO ONE WILL BE ABLE TO PREVENT A MAJOR PRICE INCREASE. BY 1980 SOME OTHER MEMBERS OF OPEC WILL HAVE INCREASED THEIR CAPACITY. SAUDI ARABIA, HOWEVER, WILL STILL HAVE SOME EXCESS CAPACITY TO PROVIDE IT WITH LEVERAGE. HOWEVER, WHEN DEMAND SURPASSES
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THE SUPPLY, THERE COULD BE AN INCREASE AS MUCH AS 40 PERCENT IN THE PRICE OF OIL BY 1980.

16. YAMANI THEN MENTIONED THAT SAUDI ARABIA STILL HAS SOME FINANCIAL PROBLEMS. FOR THE FIRST TIME ARAMCO IS NOW ASKING THE GOVERNMENT FOR MONEY TO SPEND FOR CAPITAL EXPANSION PROGRAMS. THIS IS SOMETHING OF A SHOCK TO THE SAUDI LEADERSHIP. IT WILL BE DIFFICULT FIGHT TO RAISE SAUDI PRODUCTION TO 12 MILLION BARRELS PER DAY BY THE EARLY 80'S HOWEVER, IT IS NOT UNREASONABLE TO EXPECT THAT SAUDI PRODUCTION COULD REACH 12 MILLION BARRELS BY 1983.

17. SCHLESINGER AGAIN COMMENTED THAT IS IS ESSENTIAL TO DESTROY THE MYTH IN THE WEST THAT SAUDI ARABIA WILL BE THE DUES EX MACHINA TO SOLVE ALL ENERGY PROBLEMS. THESE MYTHS MUST BE DESTROYED BEFORE WE CAN GET EFFECTIVE ACTION OUT OF THE CONGRESS. YAMANI THEN ASKED ABOUT THE CIA REPORT AND WONDERED WHAT THE MOTIVE WAS BEHIND THE PUBLICATION OF THIS REPORT. SCHLESINGER REPLIED THAT A BETTER QUESTION WAS WHETHER THERE WAS IN FACT A MOTIVE. HE POINTED OUT THAT THE CIA HAS HAD PROBLEMS WITH CONGRESS AND THE PUBLIC. IT WAS QUITE POSSIBLE THAT THE AGENCY NOW MADE MISTAKES IN THE DIRECTION OF CANDOR IN THE HOPE OF IMPROVING THEIR IMAGE.

18. SCHLESINGER THEN ASKED HOW LONG WE COULD EXPECT THE CURRENT PRICE FREEZE ON OIL TO STAY IN EFFECT. YAMANI REPLIED THAT IT TAKES AN OPEC DECISION TO CHANGE PRICES. IN THE ABSENCE OF A DECISION, THERE IS NO CHANGE. NO DECISION HAD BEEN REACHED AT CARACAS AND THUS PRICES REMAINED AS BEFORE. VENEZUELA HAD ARGUED THAT IT WOULD MAKE SENSE TO INCREASE THE PRICE OF OIL AND THEN DONATE THE INCREASED REVENUE TO THE LDC'S WHICH THEY COULD USE

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TO REDUCE THEIR DEBTS TO THE INDUSTRIAL COUNTRIES. MANY OF THE OPEC MEMBERS REFUSED TO ACCEPT THE VENEZUELAN PROPOSAL, BUT IT MAY COME UP AGAIN FOR DISCUSSION, PERHAPS IN A SPECIAL MEETING IN MARCH. SAUDI ARABIA REFUSED IN THE DECEMBER MEETING TO ACCEPT A PROPOSAL FOR A REVIEW OF PRICING AT THE JUNE MEETING. IT THEREFORE NOW APPEARS THAT THERE WILL BE A FREEZE ON OIL PRICES UNTIL THE END OF 1978.

19. AMBASSADOR WEST ASKED WHEN SUPPLY AND DEMAND FACTORS WOULD TAKE OVER AND SHARPLY INCREASE THE PRICE OF PETROLEUM. YAMANI REPLIED THAT THIS WOULD PROBABLY NOT HAPPEN IN 1978. THERE IS NO SPECULATION GOING ON NOW BECAUSE NO ONE NOW EXPECTS A PRICE INCREASE IN THE SHORT TERM. IN FACT, THERE IS NOW A SMALL EXCESS OF OIL ON THE MARKET. BY

1979, HOWEVER, WE MIGHT SEE SOME INCREASE IN SPOT MARKET
PRICES. MUCH WILL DEPEND ON IRAQ. IRAQ IS NOW PRODUCING
AT APPROXIMATELY 1.7 MILLION BARRELS PER DAY, BUT WE THINK
THEY HAVE THE CAPACITY TO PRODUCE UP TO 2.2 MILLION BARRELS
PER DAY.
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